COMPANY RESEARCH AND ANALYSIS REPORT

APPLE INTERNATIONAL CO., LTD.

2788

Tokyo Stock Exchange Second Section

8-Nov.-2017

FISCO Ltd. Analyst

Ken Segawa

FISCO Ltd.

http://www.fisco.co.jp

Index

Summary

A new growth strategy from the capital and business alliance with Isuzu Motors

Currently, APPLE INTERNATIONAL CO., LTD. <2788> (hereafter, "Apple International," also "the Company") has two main business pillars: a business for the export of used vehicles, and a business for the franchise chain headquarters for dealers of the purchase and sale of used vehicles within Japan.

1. A capital and business alliance with Isuzu Motors

On April 28, 2017, the Company entered-into a capital and business alliance with Isuzu Motors <7202>. From a payment by Isuzu Motors at the end of May, it conducted a capital increase through a third-party allocation to issue 1.38 million new shares, which corresponds to 9.97% of the total number of shares issued. In the business alliance, the two companies will collaborate in purchasing, distributing, and exporting used commercial vehicles manufactured by Isuzu Motors. Isuzu Motors manages auction sites for commercial vehicles at three locations in Chiba Prefecture, Hyogo Prefecture, and Fukuoka Prefecture, and it is expected that the Company Group's franchise chain will be used to purchase used commercial vehicles manufactured by Isuzu Motors and to list them on its auto auctions.

2. Newly establishing a subsidiary in Thailand to deploy its overseas business to the export of the used commercial vehicles manufactured by Isuzu Motors Thailand

In its overseas business, the Company plans to horizontally deploy the model that it has previously successfully established in Thailand to neighboring ASEAN countries, with Thailand as the starting point. The direction it will take for this has been made clear from the alliance with Isuzu Motors. Thailand is a major country for light commercial vehicles (LCV), where sales of one-ton pickup trucks account for more than half of domestic sales of four-wheel vehicles, and among the right-hand drive countries, Thailand is positioned second only after Japan in terms of the number of commercial vehicles produced. It seems likely that the used vehicles-exports company that the Company is preparing to establish, which will serve as its base in Thailand, will actively handle the used commercial vehicles manufactured by Isuzu Motors Thailand. Isuzu Motors overtook Toyota Motor <7203> for the cumulative number of sales of commercial vehicles in Thailand from January to August 2017 to become the country's leading producer. In addition to Thailand, the right-hand drive countries in the ASEAN Free Trade Area are Singapore, Indonesia, Brunei, and Malaysia. In Malaysia, the plan is to partner with local auction sites to develop an auto auction business, with the Company's standards as the de-facto standards. It is aiming to quickly launch businesses in new markets at low cost and low risk through utilizing the operations that achieved results in Thailand, such as the standardization of Japanese-style vehicle assessments, and the provision of an IT system that enables customers to participate in auctions via the Internet. From a business that increased profits by reading the conditions in the used vehicles market, it will increase the weight of a business model that stably generates earnings through the provision of a market infrastructure.

3. Established a subsidiary in Singapore that specializes in the repairs and maintenance of HV and EV

In August 2017, the Company established a subsidiary in Singapore that specializes in the repairs and maintenance of hybrid vehicles (HV) and electric vehicles (EV). By establishing a local, specialist maintenance company, it plans to provide a maintenance guarantee service for export vehicles in Singapore, and also to leverage synergies with its exports sales business. With an eye to the future, the Company is taking steps in advance of its industry peers to establish for overseas customers a HV and EV after-sales service, including experimental factors, as infrastructure.

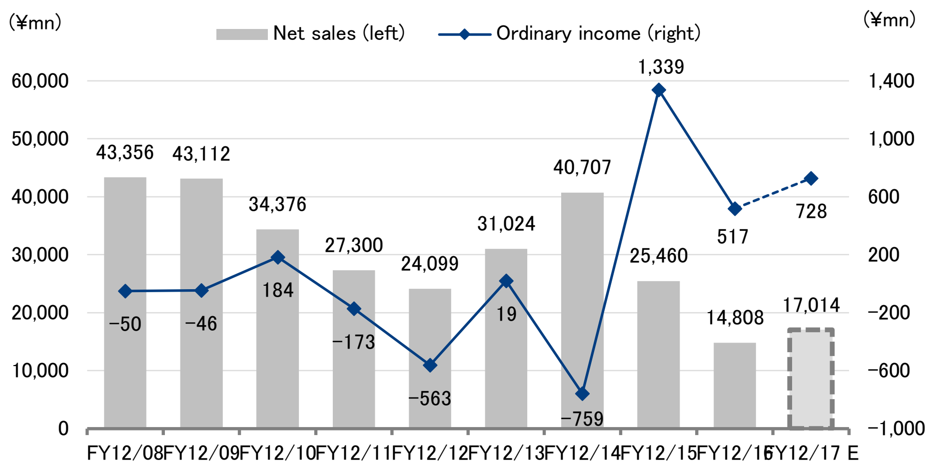
4. Domestically, the focus is on entering the rental car and car lease markets, which are ancillary business areas, rather than expanding its former businesses

In its domestic business, merely pursuing the expansion of scale in existing businesses results in added future risk due to aging populations and population decline trends in regional cities, and also from consumers focusing less on ownership and more on the use and sharing of vehicles. So the Company has adopted a business strategy of conducting new businesses in ancillary business areas. On entering FY12/17, in April it opened the first Apple Rental Car store in Naha City, Okinawa Prefecture, and then in September, it launched the Apple Lease business in directly managed stores. In the Apple Lease business, it selects models and specifications that are popular in Southeast Asia and that will therefore sell at a high price once their lease is finished. This enables it to offer vehicles that are up to 30% cheaper than the usual lease rate. It plans to differentiate itself by linking this business to the Company Group's used vehicles distribution and exports businesses, such as to Southeast Asia.

Key Points

- A new business direction from the capital and business alliance with Isuzu Motors
- In FY12/17 1H, the recovery in Thailand was offset by the decline in Singapore
- The growth strategy is to acquire business opportunities by entering-into the rental car and car lease markets

Net sales and ordinary income



Source: Prepared by FISCO from the Company's financial results

Company and business profile

Toward a new business deployment from the capital and business alliance with Isuzu Motors

1. Company profile

Apple International, as a pioneer in the export of used vehicles, launched a business to export used vehicles to Southeast Asian countries in 1996. Since then, the Company has played an important part in the automobile distribution market, not only in the buying and selling of used cars, but also establishing auto auction businesses. Overseas, the Company has continually developed new businesses based on the trust it has earned and the expanding network of human connections it has established. The main business of the Company itself in the Company Group is the export of used vehicles from Japan, while a subsidiary serves as the franchise chain headquarters in the used vehicle purchase and sale business within Japan, and a Group company also directly manages franchise dealers.

2. History

The Company was founded in Yokkaichi City, Mie Prefecture, in January 1996 for the purchase and sale of used vehicles within Japan. Subsequently, in order to respond to the needs of overseas importers following the boom in motorization in Southeast Asian countries, in December of the same year it launched a business to export used vehicles to Thailand and Hong Kong. Currently, the Company itself operates the used vehicles export business from Japan, mainly for Thailand, Malaysia, Singapore, and Indonesia.

The Company is expanding the scale and range of its operations through M&A. In November, 2001, the Company acquired shares of Car Consultant Maple Co., Ltd., which buys and sells cars, and in May 2004, it acquired shares of franchise chain headquarters Apple Auto Network Co., Ltd. (formerly Japan Automobile Distribution Network Co., Ltd.). Both of these companies are now consolidated subsidiaries.

The Company listed on the Tokyo Stock Exchange (TSE) Mothers market in December 2003, and then in May 2015, transferred to the TSE Second Section.

In November 2016, the Company established a dual-headquarters structure, setting up a second headquarters in Tokyo's Chuo Ward.

In May 2017, the Company entered-into a capital and business alliance with Isuzu Motors. It conducted a capital increase through a third-party allocation by newly issuing 1.38 million new shares (9.97% of the total shares issued) to Isuzu Motors. Both domestically and overseas, the two companies will collaborate for the purchase, distribution, and exports of the used commercial vehicles manufactured by Isuzu Motors.

History

Month and year	Major event
January 1996	Founded Apple International Co., Ltd. and started purchasing used vehicles
December 1996	Launched exports to Thailand and Singapore
July 1997	Launched exports to Hong Kong
September 1998	Launched exports to Malaysia, and then sequentially started exporting to Indonesia and other Southeast Asia countries
November 2001	Acquired shares in Car Consultant Maple Co., Ltd. and converted the company into a subsidiary
December 2003	Founded A.I.HOLDINGS (HONG KONG) LIMITED (A.I.H) in Hong Kong
December 2003	Listed on the TSE Mothers market
May 2004	Acquired shares in franchise chain headquarters Apple Auto Network Co., Ltd. and converted the company into a subsidiary
August 2004	A.I.H established a subsidiary and started dealer operations in China
August 2008	Launch of an auto auction business in Thailand from a joint-venture company (equity-method affiliate)
December 2013	The subsidiary Apple Auto Network Co., Ltd. launched a life-insurance sales business
May 2014	Sold a Chinese subsidiary BMW dealer
January 2015	Changed PRIME ON CORPORATION LIMITED and four other companies from consolidated subsidiaries to equity-method affiliates
May 2015	Transferred from TSE Mothers market to TSE Second Section
January 2016	Transferred all shares held in consolidated subsidiary IM JIHAN Corporation
February 2016	Transferred all shares held in PRIME ON CORPORATION LIMITED
November 2016	Established dual-headquarters structure by setting up a Tokyo Headquarters in Chuo Ward, Tokyo
April 2017	Opened the first Apple Rental Car store in Naha City, Okinawa Prefecture
May 2017	Resolved to liquidate A.I. HOLDINGS (HONG KONG) LIMITED, and the liquidation is scheduled to be completed by the end of November
May 2017	Entered-into a capital and business alliance with Isuzu Motors through a capital increase by a third-party allocation of shares
August 2017	Establish a subsidiary in Singapore (60% investment ratio) to repair and maintain HV and EV
September 2017	Launched a new car lease business at Apple directly managed stores with inexpensive lease fees
October 2017	Established a subsidiary in Thailand (49% investment ratio) in order to strengthen exports of used LCV

Source: Prepared by FISCO from Company materials

3. Description of business

Currently, the Company is consolidating its business into its two main business pillars, of a business for the export of used vehicles, which is conducted by the Company itself, and a business by the franchise chain headquarters for dealers for the purchase and sale of used vehicles, which is conducted by a consolidated subsidiary. The Company Group consists mainly of the Company itself, two consolidated subsidiaries, and one equity-method affiliate. The equity-method affiliate is a joint-venture company that manages auto auctions for used vehicles in Thailand.

Affiliated companies

Name	Location	Capital/amount invested	Ownership ratio		Main business activities	Comments
Apple Auto Network Co., Ltd.	Yokkaichi City, Mie Prefecture	¥347mn	74.3%	Consolidated	Used vehicle purchasing and overall management of franchise chain network	Transactions with parent
Car Consultant Maple Co., Ltd.	Nakakoma District, Yamanashi Prefecture	¥10mn	100.0%	Consolidated	Used vehicle purchasing and sales	Transactions with parent
Apple Auto Auction (Thailand) Co. Ltd.	Kingdom of Thailand	¥287mn	34.4%	Equity-method	Management of auto auction sites	Dual directorship
APPLE HEV INTERNATIONAL Pte. Ltd	Singapore	500,000 SGD	60.0%		HV and EV repairs and maintenance business	Dual directorship
APPLE INTERNATIONAL (THAILAND) Co., Ltd.	Kingdom of Thailand	2 million THB	49.0%		Exports of used commercial vehicles	Dual directorship

Source: Prepared by FISCO from Company materials

In the 2017 Oricon Japan customer satisfaction rankings, Apple was awarded first place for the fourth consecutive year in the "Vehicle purchasing companies" category. At the end of December 2016, there were 238 member dealers (including directly managed dealers) in its "Apple" franchise chain of dealers. Apple Auto Network member dealers are provided with information to help them determine appropriate price at the time of purchase including used vehicles' successful bid price information at auctions in Japan and inventory information. Through sales promotions activities utilizing the Apple brand, Apple Auto Network provides its member dealers with integrated management and in return collects royalties from them. In addition, the Company is also focusing on its property and casualty insurance counter, online insurance, and car rental businesses, all offering speedy contract completion.

In Thailand, subsidiary and joint venture with MBK Public Company Limited, Apple Auto Auction (Thailand) Co. Ltd. manages auto auction sites. Owing to foreign ownership restrictions at the time of establishment, Company's ownership is only 34.4% and the company is therefore an equity-method affiliate. The management of auction sites is a business involving the collection of exhibition fees, successful bid fees, and contract completion fees, so it is a business model in which high profits can be stably obtained if a certain level of auction volume is maintained. This subsidiary has the second highest market share (25% in 2016) in terms of dealing volumes of the auction market in Thailand. We note, however, that motorcycle sales are not included in the company's sales volume figures, although they are included in the sales volume figures of the company with the top market share (40%).

Finalizing business restructuring measures and strengthening of financial base in order to resume dividends

4. Business trends

(1) Return of the founder, restructuring of Group companies

President Yoshinobu Kubo, founder of the Company and the largest shareholder went on sick leave from 2007 and withdrew from the frontline of the Group's management. But his health recovered and in 2013 he returned to the management frontline as the Chairman and President. After his return, concerns emerged regarding the rapid expansion of operations in Asia, particularly in China, undertaken during his absence. Thereafter, he and management worked to restructure the Group. The objective of this Group restructuring was to eliminate risk factors and restore financial stability. The number of consolidated subsidiaries in FY12/09 was 28 companies and at the most, there were also 11 equity-method affiliates. This was reduced to two consolidated subsidiaries and one equity-method affiliate. The Hong Kong subsidiary and its three subsidiaries are currently inactive and undergoing liquidation procedures.

(2) Withdrawal from China business

By withdrawing from the unprofitable. China business, currency risk, market risk, and country risk relating to China have been eliminated. The Company has also improved its financial stability by ending the debt guarantee it provided to a subsidiary. The Company sold its new vehicle dealer business subsidiary in China and withdrew from the market. In FY12/09, net sales from the China business reached ¥27,194mn, which accounted for more than 60% of total sales, but since FY12/15, sales from the China has no longer been included in consolidated net sales.

Following the global financial crisis triggered by Lehman Brothers' bankruptcy in September 2008, Asian businesses suffered a significant decline in sales and recorded an enormous extraordinary loss (¥3,522mn) in FY12/09. The main reasons were an impairment loss on the goodwill of an overseas subsidiary of ¥905mn and the provision of allowance for doubtful accounts for Malaysia receivables of ¥1,101mn. In FY12/14, compared to consolidated operating income of ¥589mn, the Company recorded interest paid for non-operating expenses of ¥762mn and the provision of allowance for doubtful accounts for the Chinese subsidiary and Malaysia receivables of ¥771mn, resulting in an ordinary loss. The extraordinary loss in the same period (¥834mn) included a loss on sales of shares of subsidiary (¥310mn), and provision for loss on business of the Chinese subsidiary (¥434mn). After the Company completed the painful process of rebuilding its financial base, extraordinary losses fell to ¥2mn in FY12/15 and ¥9mn in FY12/16.

Consolidated results

(¥mn)

	FY12/07	FY12/08	FY12/09	FY12/10	FY12/11	FY12/12	FY12/13	FY12/14	FY12/15	FY12/16
Net sales	55,881	43,356	43,112	34,376	27,300	24,099	31,024	40,707	25,460	14,808
Operating income	1,217	407	-52	498	110	-169	747	589	1,322	489
Interest paid	359	261	278	201	285	326	633	762	67	30
Ordinary income	876	-50	-46	184	-173	-563	19	-759	1,339	517
Extraordinary loss	133	507	3,522	1,199	141	64	64	834	2	9
Net profit*	334	-288	-3,715	-1,604	-708	-295	50	-1,030	1,273	388

*Profit attributable to owners of parent
Source: Prepared by FISCO from Company materials

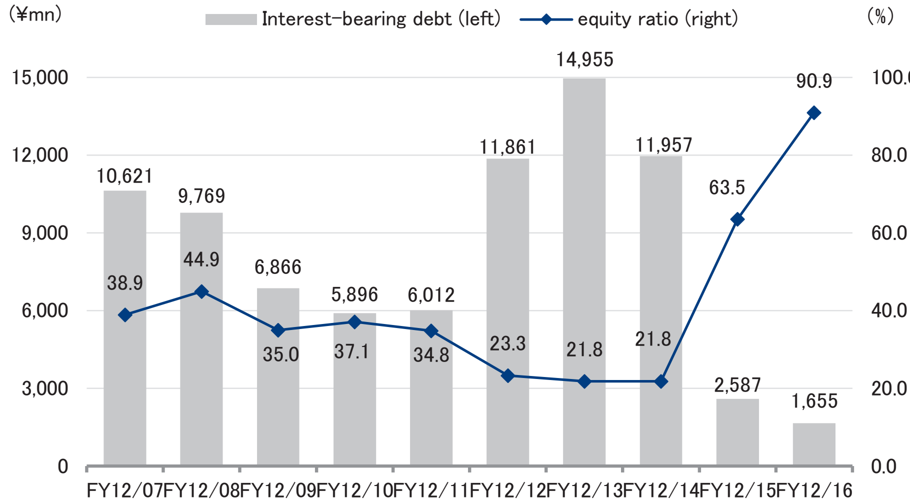
Accounts receivable at end-FY12/07 were ¥9,817mn, but by end-FY12/11, this had declined to ¥1,306mn. At end-FY12/11, long-term operating loans receivable were ¥2,379mn, long-term retained receivables were ¥1,051mn, and the allowance for doubtful accounts was ¥3,019mn, but by end-FY12/16, these had fallen to ¥682mn, ¥305mn, and ¥1,075mn, respectively. Total assets also declined from ¥29,938mn in FY12/07 to ¥7,593mn in FY12/16.

(3) Significant improvement in financial position

The Company posted net losses for five consecutive years (FY12/08-FY12/12) and interest-bearing debt rose to ¥14,955mn in FY12/13. Of the Company's ¥11,735mn in short-term borrowing as of end-FY12/14, China-related borrowing accounted for ¥10,513mn, and in terms of financing, this business had become a factor hampering the development of other businesses. As China-related borrowing was eliminated by end-FY12/15, interest-bearing debt declined greatly, from ¥11,957mn of end-FY12/14 to ¥2,587mn. In FY12/16, interest-bearing debt was reduced and moreover, short-term borrowing was repaid and replaced with long-term borrowing.

Looking at ratios related to financial stability, the current ratio, which indicates a company's ability to pay its short-term debts, rose from 115.4% in end-FY12/13 to 617.2% in end-FY12/16, well above 200%, the level considered ideal. Over the same period of time, the equity ratio, which indicates a company's ability to pay its long-term debts, rose from 21.8% to 90.9%, above the ideal level of 70%.

Interest-bearing debt and equity ratio



Source: Prepared by FISCO from Company materials

(4) Finalizing business restructuring measures and strengthening of financial base in order to resume dividends

In FY12/16, consolidated retained earnings had improved from negative ¥292mn at the end of FY12/15 to positive ¥1,209mn, erasing accumulated losses. However, parent retained earnings remained in deficit, which was an obstacle to the resumption of dividends. Therefore, at the General Meeting of Shareholders held in March 2017, the Company decided to reduce capital reserves by ¥694mn and appropriate this amount to write off negative retained earnings as the final step in its restructuring program. We therefore believe the Company has strengthened its financial base enough to resume dividend distributions in FY12/17.

Results trends

In FY12/17 1H, the recovery in Thailand was offset by the decline in Singapore

1. Overview of FY12/15 and FY12/16 results

(1) FY12/15 results: Strong profit growth partly owing to rush demand in Thailand

In FY12/15, the Company performed so much better than expected that it upwardly revised its forecasts twice in 2H. Net sales surpassed initial forecasts by 58.9%, operating income outperformed by 144.0%, and ordinary income was 294.1% above target. Looking at FY12/15 results, net sales were down 37.5% YoY to ¥25,460mn, operating income rose 124.2% to ¥1,322mn, ordinary income was ¥1,339mn, and profit attributable to owners of parent was ¥1,273mn. The reason for the major decline in sales YoY was that the subsidiary in the China business was removed from the scope of consolidation and became an equity-method affiliate. The Company carried out measures to increase profitability and rush demand in Thailand ahead of the implementation of the change in the vehicle tax system in January 2016 also boosted earnings.

(2) FY12/16 results: fell short of initial forecast owing to three negative factors

FY12/16 results fell short of the Company's initial forecast owing to three negative factors. The first factor was an increase in the vehicle tax in Thailand, the largest export destination for the Company's used vehicles. The second factor was yen appreciation around midyear. The third was the mood of self-restraint in Thailand regarding leisure activities and consumption owing to the passing of the Thai king in October.

The Company's initial forecast was for declines in sales and income owing to the temporary bringing forward of demand in the latter half of FY12/15. The initial forecasts were for net sales to fall 32.3% YoY to ¥17,232mn, ordinary income to decrease 32.1% to ¥910mn, and profit attributable to owners of parent to fall 44.9% to ¥702mn. The sales decline was expected owing to the sale of all of the Company's shareholdings in IM JIHAN Corporation in January 2016 and in PRIME ON CORPORATION LIMITED (Hong Kong) in March. The Company posted an extraordinary gain from the sale of shares in its affiliated companies of ¥97mn.

In FY12/16, net sales declined 41.8% YoY to ¥14,808mn, operating income fell 63.0% to ¥489mn, ordinary income fell 61.4% to ¥517mn, and profit attributable to owners of parent fell 69.5% to ¥388mn. Sales fell short of the Company's initial estimate by 14.1%, ordinary income fell short by 43.2%, and profit attributable to owners of parent was 44.7% below forecast.

a) Revisions to the import vehicle excise tax system in Thailand

Starting in January 2016, Thailand began determining the vehicle tax rate based on CO2 emissions rather than engine displacement volume. This triggered demand at the end of 2015 in advance of the implementation of the revision to the tax system, and as a reaction to this, sales declined YoY during the 1Q FY12/16. Unexpectedly, it took time to clarify standards for imported vehicles and this had the accelerated negative impact on 1H results. While the tax rate was reduced for eco-cars, in general, it was raised for all other cars.

Revisions to the Thai vehicle excise tax

Vehicle type	Previous system				New system			
	Displacement volume	Tax rate			CO_2 emission volume	Tax rate		
		E10	E20	E85		E10/E20	E85/NGV	Hybrids
Eco-car E85	1,300/1,400cc		17		Less than 100g/km		14/12	
					101-120g/km		17/17	
Passenger vehicles	2,000cc or lower	30	25	22	100g/km or lower	30	25	10
	2,001-2,500cc	35	30	27	101-150g/km			20
	2,501-3,000cc	40	35	32	151-200g/km	35	30	25
	3,001cc or higher	50	50	50	201g/km or higher	40	35	30
					3,000cc or higher	50	50	50
Pickup trucks	3,250cc or lower		3, 18		200g/km or lower		3, 18	
					201g/km or higher		5, 18	
	3,251cc or higher		50		3,251cc or higher		50	

Source: Prepared by FISCO from various materials

b) Yen appreciation from midyear until summer

Yen appreciation also had a negative impact on earnings. In June-August, the yen strengthened to below ¥100/USD, which was the strongest it had been since November 2013. Comparing exchange rates at end-FY12/15 with end 2Q FY12/16 (end-June), the yen strengthened 13.2% against the US dollar, 11.5% against the Thai baht, and 9.9% against the Singapore dollar. As sales in Thailand slumped due to the revision to the tax system, the Company focused on exports to Singapore and these exports grew despite the strong yen. However, rapid exchange rate fluctuations can cause consumers to adopt a wait-and-see approach and to defer payments. Rather than pursue sales growth, the Company continued to focus on achieving stable earnings through sound business operations.

c) Passing of the Thai King

Thai King Bhumibol, deeply loved by the Thai people, passed away at age 88 in October 2016. In his reign of over 70 years, King Bhumibol became dear to the hearts of the Thai people and, after his passing, a mood of self-restraint pervaded in the country regarding leisure activities and consumption. In December 2016, Prince Vajiralongkorn officially ascended to the throne. After a one-year period of mourning, the cremation of the late king will be conducted on October 26, 2017 and the new king will be crowned following the ceremony.

d) Domestic used auto purchase and sale business

In FY12/16, sales in the used auto purchase and sale business rose 14.8% YoY to ¥5,337mn. Average sales per directly managed dealership rose 5.2% to ¥245mn. The number of franchise dealerships remained steady YoY at 238. The total number of assessments conducted by chain dealers declined by 3.3% to 154,400 vehicles, the number of vehicles purchased declined by 4.7% to 73,600 units, and the number of vehicles sold fell by 3.1% to 78,900, with the number of retail sales down 1.0% to 9,900.

The used vehicles purchase and sale business

(Vehicles)

	FY12/14	FY12/15	FY12/16	YoY	
				Increase	Growth rate
No. of FC dealers (dealers)	225	238	238	0	0.0%
No. of assessments	147,800	159,700	154,400	-5,300	-3.3%
No. of vehicles purchased	72,800	77,200	73,600	-3,600	-4.7%
No. of vehicles sold	75,400	81,400	78,900	-2,500	-3.1%
Of which, no. of vehicles sold at auction	66,200	71,400	69,000	-2,400	-3.4%
Of which, no. of retail-sales vehicles	9,200	10,000	9,900	-100	-1.0%

Source: Prepared by FISCO from Company materials

2. Overview of FY12/17 1H consolidated results

(1) Summary of the FY12/17 Q2 results – the recovery in Thailand was offset by the slump in Singapore

In the FY12/17 1H consolidated results, net sales increased 2.4% YoY to ¥7,044mn, operating income decreased 12.1% to ¥224mn, ordinary income increased 17.8% to ¥239mn, and profit attributable to owners of parent rose 35.2% to ¥141mn. Compared to the initial forecast, net sales were down 21.2%, operating income was down 42.3%, ordinary income was down 36.1%, and profit attributable to owners of parent was down 52.6%.

FY12/17 1H results

(¥mn)

	FY12/16 1H		FY12/17 1H				
	Results	% of sales	Initial forecast	Results	% of sales	YoY	vs. forecast
Net sales	6,878	-	8,940	7,044	-	2.4%	-21.2%
Gross profit	996	14.5%	-	950	13.5%	-4.7%	-
SG&A expenses	741	10.8%	-	725	10.3%	-2.2%	-
Operating income	255	3.7%	390	224	3.2%	-12.1%	-42.3%
Ordinary income	203	3.0%	375	239	3.4%	17.8%	-36.1%
Profit attributable to owners of parent	104	1.5%	299	141	2.0%	35.2%	-52.6%

Source: Prepared by FISCO from Company materials

Exports of used vehicles to Thailand have been recovering, as the three factors that caused them to worsen in FY12/16 have weakened. On the other hand, exports to Singapore, which covered for the slump in Thailand in FY12/16, have fallen, and this has offset the recovery in Thailand.

In the domestic franchise business, although new member dealerships were acquired, there was around the same number of withdrawals. Gulliver (IDOM <7599>), BIGMOTOR (BIGMOTOR Co., Ltd.) and Nextage <3186> are actively expanding their networks through directly managed dealerships, and the competition in the market for dealerships specializing in auto purchasing has intensified.

(2) Balance sheet and cash flow

At the end of FY12/17 Q2, total assets were up ¥968mn on the end of previous fiscal year to ¥8,561mn. This was mainly due to increases in cash and deposits and in accounts receivable.

At the end of FY12/17 Q2, the balance of cash and cash equivalents was up ¥364mn on the end of the previous fiscal year to ¥2,732mn. Cash flow used in operating activities was ¥94mn, as while net income before income taxes was ¥239mn, trade receivables increased ¥294mn and inventory assets rose ¥97mn. Cash flow from financing activities was ¥597mn, as although there were expenses of ¥181mn for the repayment of long-term debt, there was income of ¥375mn from the increase in short-term debt, and of ¥398mn from the issue of shares.

The indicators of financial stability are at extremely high levels, as the current ratio is 413.7% and the equity ratio is 84.2%.

Balance sheet

(¥mn)

	FY12/13	FY12/14	FY12/15	FY12/16	FY12/17 Q2	Change
Cash and deposits	12,464	9,397	2,533	2,429	2,905	475
Accounts receivable – trade	2,220	3,632	3,472	3,204	3,498	294
Merchandise	3,808	3,583	732	869	956	87
Accounts receivable – other	2,226	2,013	538	3	3	0
Allowance for doubtful accounts	-	-	-	-	-109	-2
Current assets	21,221	18,853	7,856	6,905	7,884	978
Property, plant and equipment	844	753	215	237	237	-0
Intangible assets	26	29	42	40	33	-6
Investments and other assets	2,017	1,026	990	409	406	-2
Non-current assets	2,889	1,809	1,248	687	677	-9
Total assets	24,110	20,662	9,104	7,593	8,561	968
Current liabilities	18,397	16,629	4,872	1,118	1,905	786
Non-current liabilities	268	209	282	1,254	1,051	-203
Total liabilities	18,666	16,838	5,154	2,373	2,957	583
(Interest-bearing debt)	14,955	11,957	2,587	1,655	2,013	357
Net assets	5,444	3,824	3,950	5,219	5,604	385
Total liabilities and net assets	24,110	20,662	9,104	7,593	8,561	968
Ratios of stability						
Current ratio	115.4%	113.4%	161.2%	617.2%	413.7%	
Equity ratio	21.8%	21.8%	63.5%	90.9%	84.2%	

Source: Prepared by FISCO from the Company's financial results

Outlook

The FY12/17 full year forecasts have been left unchanged

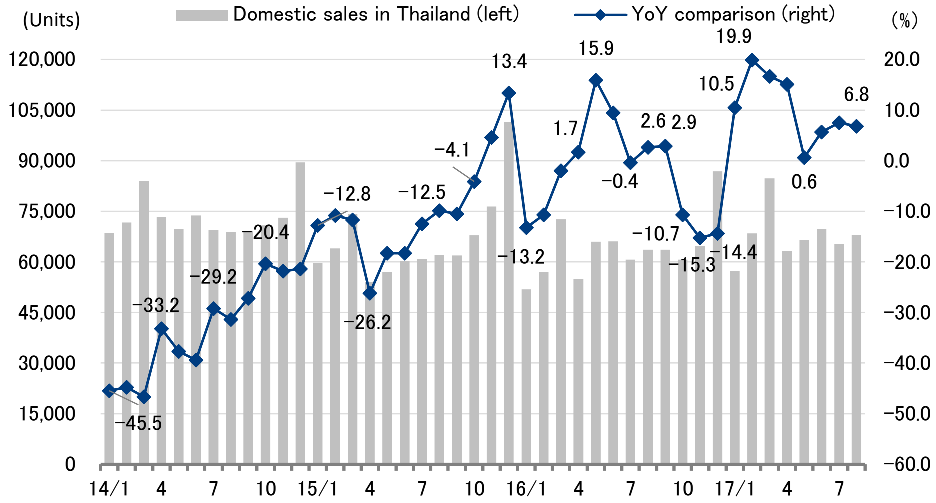
In FY12/17, the Company forecasts consolidated net sales of ¥17,014mn, up 14.9% YoY, operating income of ¥685mn, up 40.1%, ordinary income of ¥728mn, up 40.8%, and profit attributable to owners of parent of ¥576mn, up 48.3%.

(1) Upturn in Thai market

Thai automobile sales volume showed double-digit YoY decline for three consecutive months starting in October 2016 when the former king passed away. We saw signs of a recovery in 2017, with sales volume growing 10.5% YoY in January and 19.9% in February, partly owing to weak sales in January-February 2016 resulting from revisions to the vehicle tax system. Although the growth rate subsequently slowed down, it did not once go below the level of the previous year, and in August, it increased 6.8% compared to the same month in the previous fiscal year. In terms of the reasons for this strong performance, the Federation of Thai Industries cited the launch of new models, the rise in the number of tourists, the increase in agricultural production, the expansion of exports, and the growth in private sector capital investment.

The funeral of the former king will be held for five days, from October 25 to 29. People are expected to show restraint during this funeral period, such as for eating and drinking or how they dress. Conditions will return to normal in FY12/18 and the business environment is expected to improve.

The number of four-wheel vehicles sold in Thailand and YoY growth rate comparison



Source: Prepared by FISCO from various materials

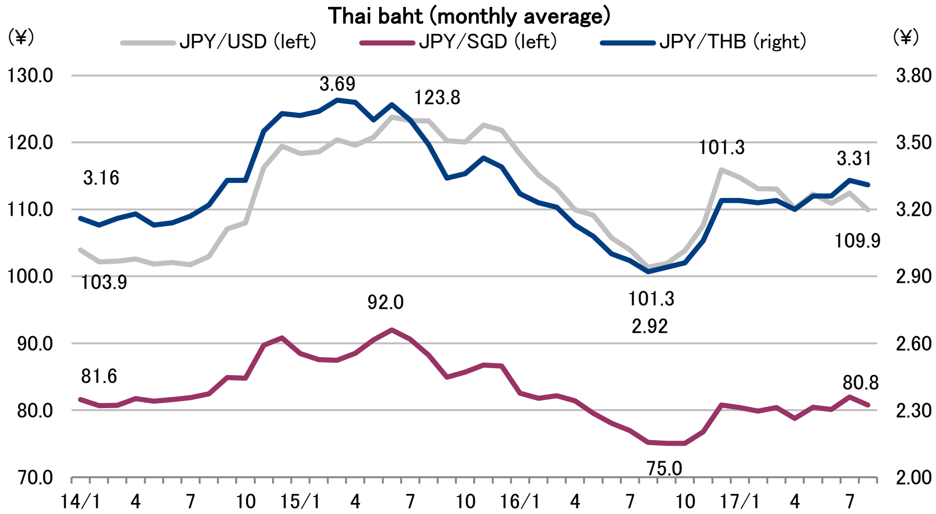
(2) Established a subsidiary in Singapore specializing in HV and EV repairs and maintenance

The recovery in Thailand in FY12/17 is being offset by the slump in Singapore, but the Company is still implementing measures to expand its business in this country. In August 2017, it established a subsidiary in Singapore specializing in the repairs and maintenance of HV and EV. Including in Singapore, consumers in Asian countries have tended to avoid HV and EV for many years, due to their concerns about their repairs and maintenance. By establishing a local, specialist maintenance company, the Company plans to provide a maintenance guarantee service for export vehicles in Singapore, and also to leverage synergies with its exports sales business. Its investment ratio in the new subsidiary, which is called APPLE HEV INTERNATIONAL Pte. Ltd., is 60%, with the remaining 40% being invested by a local company. HEV Shop Pte. Ltd, which is the joint investor, has conducts a business in Singapore specializing in the repair and maintenance of HV and EV. With an eye to the future, the Company is taking steps in advance of its industry peers to establish for overseas customers a HV and EV after-sales service, including experimental factors, as infrastructure.

(3) Expect exchange rate to remain roughly the same as in FY12/16

The Company expects the exchange rate in FY12/17 to be roughly the same as in FY12/16 of ¥110/USD. In 1H, the exchange rates between the Japanese yen and the U.S. dollar, Singapore dollar, and Thai baht all remained stable and tended toward depreciation in Japanese yen until now from end-FY12/16 levels, resulting in a more favorable business environment than in FY12/16.

Exchange rates vs. yen for U.S. dollar, Singapore dollar, and Thai baht (monthly average)



Source: Prepared by FISCO from various data

(4) Progress made in 1H

In the initial forecasts for FY12/17, the Company planned to earn around 52% of the full year forecasts for both net sales and ordinary income by the end of Q2. The 1H results did not reach the initial forecasts and they have been left unchanged, as the rates of progress for the forecasts in 1H were 41.4% for net sales and 32.9% for ordinary income. At the end of Q2, accounts receivable had increased and payments from overseas customers were stagnant, and in such a situation, it will be difficult to promote sales.

(5) Extraordinary gains

The FY12/17 profit attributable to owners of parent is expected to correspond to less than 80% of ordinary income. It is anticipated that the recovery of receivables in Southeast Asia, for which an allowance for doubtful accounts was accumulated in the past, and the receivables owned by its Chinese subsidiary, will be recorded as extraordinary income from company liquidation. In May 2017, the Company resolved to liquidate its consolidated subsidiary A.I. HOLDINGS (HONG KONG) LIMITED, and the liquidation is scheduled to be completed by the end of November. Although the collection of receivables is currently being disputed in court, if the ruling is completely in favor of the Company, it may record more extraordinary income than expected. Also, although it will depend on the exchange rate at that time, if the rate stays at its current level, it is expected to record a large foreign currency translation gain in non-operating income. In the current business situation, accounts receivable for Singapore are accumulating and recovering the shortfall from 1H in 2H is likely to be difficult. But even so, the Company has not changed its full fiscal year forecasts, as it expects to record temporary income, including a gain on foreign currency.

Medium-to-long-term growth strategy

A new business direction from the capital and business alliance with Isuzu Motors

1. The capital and business alliance with Isuzu Motors

In May 2017, the Company entered-into a capital and business alliance with Isuzu Motors. For the capital alliance, it conducted a capital increase through a third-party allocation by issuing 1.38 million new shares (9.97% of the total shares issued; issue price per share, ¥291). For the business alliance, both companies are currently formulating specific measures, but domestically they will promote the purchase and distribution of used commercial vehicles manufactured by Isuzu Motors through the franchise chain being developed by Apple Auto Network. Overseas, they will collaborate to expand the sales channels for used vehicle exports, including to emerging countries, in the business for the LCV (pickup trucks) manufactured by Isuzu Motors Thailand.

Isuzu Motors manages Isuzu Motor Auctions at three sites in Japan; the Makuhari site in Chiba Prefecture, the Kobe site in Hyogo Prefecture, and the Kyushu site in Fukuoka Prefecture. It is expected that the used commercial vehicles manufactured by Isuzu Motors will be purchased by the Company Group's franchise chain and listed on its auctions.

A capital and business alliance with Isuzu Motors

Details of the capital alliance	
Number of shares issued	1.38 million shares (corresponding to 9.97% of the total number of issued shares)
Form	Private placement
Allocated to:	Isuzu Motors Limited
Issue price	¥291 per share
Payment date	May 31, 2017
Details of the business alliance	
In Japan	They will collaborate for the purchase and distribution of used commercial vehicles manufactured by Isuzu Motors using the franchise chain being developed by a subsidiary (Apple Auto Network)
Overseas	They will collaborate to expand sales channels for exports of used vehicles, including in emerging countries, for the business of the LCV (pickup trucks) manufactured by Isuzu Motors Thailand

Source: Prepared by FISCO from press releases

2. Isuzu Motors and the overseas business

The Company is preparing to establish a used vehicles export company in Thailand. The current capital and business alliance indicates the direction it will take for this company, of it actively handling the used commercial vehicles manufactured by Isuzu Motors Thailand.

(1) Right-hand drive countries

The countries that are right-hand drive, the same as Japan, are the British Commonwealth countries. In ASEAN, of which Thailand is a member, the right-hand drive countries are Singapore, Indonesia, Brunei, and Malaysia. The ASEAN Free Trade Area (AFTA) was upgraded to the ASEAN Economic Community (AEC) in December 2015, and tariffs between member countries have been eliminated since 2016. The member countries are Thailand, Singapore, Malaysia, Indonesia, the Philippines, Brunei, Vietnam, Myanmar, Laos, and Cambodia. Even among them, Thailand is a hub for the automotive manufacturing industry in Southeast Asia.

Right-hand drive countries

Region	County
Asia	Macau, Hong Kong, Japan
Southeast Asia	Indonesia, Singapore, Thailand, Brunei, Malaysia, East Timor
South Asia	India, Sri Lanka, Nepal, Bangladesh, Pakistan, Bhutan, Maldives
Oceania	Oceania Australia, Kiribati, the Cook Islands, the Solomon Islands, Tuvalu, Nauru, Niue, New Zealand, Papua New Guinea, Fiji, American Samoa
Africa	Africa Uganda, Kenya, Zambia, Zimbabwe, Swaziland, Seychelles, Tanzania, Namibia, Botswana, Malawi, Mozambique, Mauritius, Lesotho, South Africa
The Middle East	Cyprus
Europe	Ireland, United Kingdom, Malta
South America	Guyana, Suriname

Source: prepared by FISCO from various materials

According to global auto statistics from OICA (the Organisation Internationale des Constructeurs d'Automobiles) the number of four-wheel vehicles registered and sold in 2016 was 93.85 million vehicles. Breaking this down, there were 69.46 million passenger vehicles, and 24.39 million commercial vehicles. Right-hand drive countries accounted for 16.74 million vehicles, or 17.8%, of this total, of which, 3.30 million, or 19.8%, were commercial vehicles. By region, demand for commercial vehicles in right-hand drive countries was concentrated in Asia, Oceania and the Middle East, which accounted for 2.64 million vehicles, or about 80%, of the total.

The global number of four-wheel vehicles registered and sold (2016)

(1,000 units)

	Passenger vehicles	Commercial vehicles	Total	Passenger vehicles	Commercial vehicles	Total
The world						
Europe	17,292	2,843	20,135	24.9	11.7	21.5
The USA	11,746	13,803	25,549	16.9	56.6	27.2
Asia, Oceania, and the Middle East	39,445	7,413	46,858	56.8	30.4	49.9
Africa	981	333	1,314	1.4	1.4	1.4
Subtotal	69,464	24,392	93,856	100.0	100.0	100.0
Of which, right-hand drive countries						
Europe	2,859	465	3,324	21.3	14.0	19.9
The USA	5	1	6	0.0	0.0	0.0
Asia, Oceania, and the Middle East	10,192	2,640	12,832	75.9	79.8	76.6
Africa	378	203	582	2.8	6.1	3.5
Subtotal	13,434	3,309	16,744	100.0	100.0	100.0

Source: Prepared by FISCO from OICA statistics

(2) The importance of right-hand drive vehicles in Thailand

Looking at the numbers of vehicles produced in 2016 by right-hand drive countries, Japan was the top at 9.2 million vehicles, followed by India at 4.48 million, and then Thailand was third at 1.94 million. But when limited to commercial vehicles, this becomes 1.33 million in Japan, followed by 1.13 million in Thailand, and then 810,000 in India. Toyota Motor has ended sales within Japan of its Hilux pickup truck, which is its strategic vehicle for emerging countries, but it announced that it will restart the import of vehicles made in Thailand in September 2017 for the first time in 13 years. So the importance of right-hand drive commercial vehicles in Thailand is high.

No. of four-wheel vehicles produced in right-hand drive countries (2016)

	Passenger vehicles (1,000 units)	Commercial vehicles (1,000 units)	Total (1,000 units)	Passenger vehicles (%)	Commercial vehicles (%)	Total (%)
Japan	7,874	1,331	9,205	49.7	34.2	46.6
India	3,678	811	4,489	23.2	20.8	22.7
Thailand	805	1,139	1,944	5.1	29.3	9.8
United Kingdom	1,723	94	1,817	10.9	2.4	9.2
Indonesia	968	209	1,177	6.1	5.4	6.0
South Africa	336	263	599	2.1	6.8	3.0
Malaysia	470	44	513	3.0	1.1	2.6
Subtotal	15,854	3,892	19,744	100.0	100.0	100.0
Right-hand drive countries	15,853	3,892	19,744	21.8	16.9	20.7
Left-hand drive countries	56,734	19,090	75,824	78.2	83.1	79.3
Total	72,587	22,982	95,569	100.0	100.0	100.0

Source: Prepared by FISCO from OICA statistics

In emerging countries, there is considerable demand for pickup trucks that can carry people and cargo at the same time. According to the Federation of Thai Industries, 1.944 million of these trucks were produced in 2016, of which, 769,000 were sold domestically and 1.189 million were exported. Within the domestic sales, commercial vehicles accounted for more than half, at 489,000 vehicles. Furthermore, of this number, 394,000 vehicles, or 51.3% of the total, were actually one-ton pickup trucks.

(3) Isuzu Motors are No.1 for sales of one-ton pickup trucks in Thailand

Thailand is a right-hand drive country and its market is dominated by Japanese manufacturers. In the percentages of vehicle sales by manufacturer and brand in 2016, the top was Toyota Motor with 31.8%, followed by Isuzu Motors with 18.6%, and third was Honda Motor <7267> with 14.0%. Below them were Mitsubishi Motors <7211> with 7.2%, Nissan Motor <7201> with 5.6%, Mazda Motor <7261> with 5.5%, Ford (USA) with 5.3%, Suzuki <7269> with 3.0%, Chevrolet (USA, GM) with 1.9%, Hino Motors <7205> with 1.7%, and others, with 5.4%. This meant that Japanese manufacturers accounted for 87.4% of the total.

When limited to the one-ton pickup truck, for the cumulative number of vehicles sold from January to August 2017, Isuzu Motors had the top share with 35.1%. Next was Toyota Motor with 31.1%, and third was Ford (12.2%).

Looking at the trends in market shares by manufacturer and brand for commercial vehicles, including one-ton pickup trucks and SUVs, in 2012 a large gap had opened up between Toyota Motor with 38.1% and Isuzu Motors with 27.9%. But subsequently this gap narrowed, and by 2016 it had become 32.1% to 29.3%. In cumulative sales from January to August 2017, Isuzu Motors was top with 31.1%, overtaking Toyota Motor (26.7%).

Among the cumulative vehicle sales from January to August 2017 by manufacturer and brand, the percentages of sales provided by one-ton pickup trucks was 91.3% for Isuzu Motors, but 57.0% for Toyota Motor. The reliance of Ford and Chevrolet on the one-ton pickup truck is also high, at 93.4% and 95.5% respectively.

From the current capital and business alliance, Isuzu Motors expects not only transactions for used one-ton pickup trucks manufactured in Thailand to become more active at the auction sites managed by the Group companies, but also for sales channels for exports to expand. The expansion of sales channels will increase the value of used vehicles and will eventually promote sales of new vehicles. On the other hand, in the distribution of used vehicles, for which purchases are the key to success, it has become easier for the Company Group to purchase the popular Isuzu Motors vehicles manufactured in Thailand. In addition to the increase in the number of vehicles being listed in its auctions site business, it expects the alliance to expand the volume of transactions for the vehicles-exports company that the Company is currently preparing to establish in Thailand.

3. Business deployment to ASEAN countries

The Company plans to horizontally deploy the business model that has proven successful in Thailand to its neighboring right-hand drive countries. The Company Group has the largest network of auto auction sites in Thailand. For auto auctions, it is important that the assessments of the vehicles to be listed are carried out objectively. The Company has standardized vehicles assessments through its used vehicles purchasing operations in Japan, its export of used vehicles from Japan, and the management of its auction sites in Thailand. Going forward, it will horizontally deploy the business model that has proven successful in Thailand to its neighboring countries. In countries where an auto auction business that utilizes IT systems has not yet been established, the Company is aiming to enter-into these countries at an early stage and to establish its own assessment criteria as the industry de-facto standard, and to spread its auto auctions management business that is based on its IT systems.

Currently, it is progressing the establishment of an auto auction business-related subsidiary in Malaysia, with the goal of establishing it within the year. In Thailand, more than 80% of vehicles to be auctioned are from financial institutions, so it is partnering with the Thanachart Bank Group in this country. In Malaysia, it is looking to form partnerships with local companies that already have auto auction sites. This method enables it to omit the time that would be required to purchase the land on which to establish the auction site locally and to build the new facilities, and it therefore allows it to launch a business in a short period of time. It also enables the Company to specialize in its strengths, such as the standardization of assessments, and in the management of IT systems. Needs are high for a bidding function via the Internet that allows customers to bid without having to physically go to the auction site. The Company can utilize its facilities in Thailand for the IT system, and therefore it anticipates being able to stably generate earnings, including auction fees and system-usage fees, from little capital and at low risk. After the business deployment in Malaysia, it is likely to consider entering-into other right-hand drive countries, such as India and Indonesia.

4. Domestic businesses

Looking at the auto distribution business in Japan, in addition to the declining and aging population, the price of vehicles is rising owing to more demanding environmental and safety standards and volume growth in the Japanese new car and used car markets is therefore not likely. In the absence of growth in the auto market, many companies have adopted growth strategies involving expanding into ancillary business domains occupied by rivals. For example, companies in the used vehicle purchase business have moved into retail and used car sellers have launched foreign-made new car dealerships and dealerships specializing in auto purchasing.

Rather than simply pursuing the expansion of volume in a contracting market, the Company is developing schemes for its franchise business, including for rental car and car lease businesses, and it is aiming to diversify its revenue sources by leveraging synergies with the Company Group's existing functions. On entering FY12/17, in April it opened the first Apple Rental Car store in Naha City, Okinawa Prefecture, and then in September, it launched the Apple Lease business in directly managed stores at inexpensive lease rates.

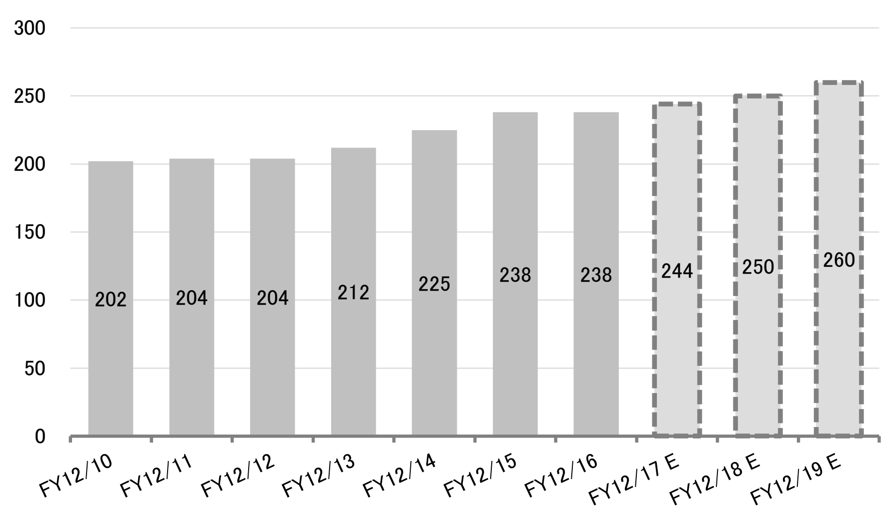
(1) Changes in the business environment

Based on the changes the Company expects to see in the future business environment, it believes that it would be risky to merely pursue volume growth in its existing businesses. The Masuda Report published by private research organization Japan Policy Council in May 2014 included a list of 896 municipalities–about half of the 1,800 municipalities in Japan--that are in danger of disappearing because of declining birthrates and population decline in the 30-year period starting in 2010. In March 2017, it was reported that over 300 cities, towns, and villages were planning to become “compact cities” by systematically downsizing while maintaining functionality as local governments. While there have been few successful transitions into compact cities, amid population decline and an increase in the number of municipalities experiencing the “doughnut effect” wherein the city center becomes “hollow”, it is becoming increasingly difficult to maintain local urban functionality including public services, medical, welfare, and commercial functions. Until recently, Japanese urban policy has focused on the development of suburbs, but the time has come for national and local governments to reconsider this focus.

(2) Revision of target number of dealerships

The number of Apple member dealers, including directly managed dealers, increased by 13 in FY12/15 and the plan was to increase the number by 13 again in FY12/16 and to reach 300 in FY12/17. In FY12/16, however, the total number of dealerships stayed the same because the same number of dealerships left the franchise association as joined it. The Company currently targets 260 dealerships by FY12/19. The original plan to increase the number of dealerships by establishing suburban roadside dealerships on national highways was changed because it was decided this type of expansion could cause problems in the future. However, the Company is looking into a number of other possibilities. For example, it plans to increase the number of shop-in-shop format dealerships which are tenants in shopping centers that attract high customer traffic. In December 2015, the Company opened a shop-in-shop format Kuruma Kaitori Hanbai Apple dealership in la Flore Hashimoto, a community based shopping center in Sagamihara City, Kanagawa Prefecture. If this format is successful, we expect the Company to once again target a total of 300 dealerships.

Number of Apple member dealers



Source: Prepared by FISCO from Company materials

(3) Expanding into rental car business

Among the younger generation of Japanese people, consumption trends are shifting from a focus on products and physical objects to a focus on services and experiences and from possession (exclusive ownership) to sharing (communal use). In the cloud computing era, the focus has shifted from resource ownership to use of resources. In the US music industry, fixed-rate music distribution services now outsell music CDs and file download sales. In the auto market, the movement away from cars by younger people has evolved into a change in focus from car ownership to car usage.

The Company Group is promoting the packaging of its rental car business in order to respond to the development of the sharing economy. In this business also, it plans to develop a franchise chain under the Apple brand. New cars are normally used for rental cars, but the Company will also utilize used cars. It has already investigated a rental car business that utilizes used cars in Thailand. In Okinawa, where the number of visitors to Japan is increasing due to the effects of inbound demand, in April 2017 it opened Apple Rental Car Naha as the first member store in the franchise. The second store is planned for Sapporo City, Hokkaido, where inbound-demand effects are also expected. However, as demand declines dramatically in the winter when it snows, it will need to responsively adjust the vehicles it holds according to the season.

(4) Entering-into the car lease business

In April 2017, the Company launched a car lease business for individuals utilizing the used vehicles that it owns. Further, in September, it added new vehicles to the menu. The business has been launched from 10 directly managed stores in Chiba City and Fujisawa City, Kanagawa Prefecture, in addition to in Yokkaichi City, Mie Prefecture, which is the location of the Company's head office, and in Suzuka City and Ise City. From this fall, it plans to expand the franchise network to approximately 200 stores nationwide, while it is aiming to lease 2,000 vehicles by the start of the year, and 10,000 vehicles nationwide by five years after that.

The point of differentiation for the Company's new vehicle leases is that it selects models that are popular in overseas markets, particularly in Southeast Asia, and therefore it is able to keep down the lease fees on the assumption that the vehicle will be purchased at a high price after the lease contract has ended. There are cases in which it can charge lease fees 30% cheaper than usual fees. In terms of the vehicles it will lease, there are around 10 models, including Toyota Motor's luxury minivan Alphard, Vellfire, the compact minivan Sienta, Nissan's Serena, and Honda's Vezel. In the case of a five-year lease, the monthly lease fee is ¥38,000 for the Vellfire and ¥25,000 for the Sienta. If customers sell the vehicle that they currently own and allocate that money to a down payment, the lease fee is further reduced. The lease fee includes automobile tax, acquisition tax, weight tax, mandatory vehicle liability insurance, vehicle inspection expenses, and various other expenses. The additional financial burden on the user is a five-year optional insurance. For the Company, the handling fee for the optional insurance is included in income.

The key point for the car lease business is that the monthly lease fee is low, so for the customer, in terms of cost, it is more advantageous to lease than to buy. If the customer selects the Suzuki Alto L mini-car, the down payment is zero and the monthly lease fee for five years is less than ¥10,000, at ¥7,776. If the Honda N-BOX G is chosen, the fee becomes ¥10,800.

Shareholder return policy

Finished shoring up financial base in order to resume dividends

As mentioned above, the Company completed measures to shore up its financial base in order to resume dividends in FY12/17 by appropriating capital to write off negative retained earnings at the parent. The Company's initial forecast is for net income per share of ¥46.27, but we believe the possibility that the Company could post extraordinary gains should also be considered. Isuzu Motors has newly become the leading shareholder, so it can be said that the likelihood that dividends will be resumed has increased.

Disclaimer

FISCO Ltd. (the terms “FISCO”, “we”, mean FISCO Ltd.) has legal agreements with the Tokyo Stock Exchange, the Osaka Exchange,and Nikkei Inc. as to the usage of stock price and index information. The trademark and value of the “JASDAQ INDEX” are the intellectual properties of the Tokyo Stock Exchange, and therefore all rights to them belong to the Tokyo Stock Exchange.

This report is based on information that we believe to be reliable, but we do not confirm or guarantee its accuracy, timeliness,or completeness, or the value of the securities issued by companies cited in this report. Regardless of purpose,investors should decide how to use this report and take full responsibility for such use. We shall not be liable for any result of its use. We provide this report solely for the purpose of information, not to induce investment or any other action.

This report was prepared at the request of its subject company using information provided by the company in interviews, but the entire content of the report, including suppositions and conclusions, is the result of our analysis. The content of this report is based on information that was current at the time the report was produced, but this information and the content of this report are subject to change without prior notice.

The final selection of investments and determination of appropriate prices for investment transactions are decisions for the recipients of this report.

FISCO Ltd.